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Author(s): Willard Straight

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CHINA'S LOAN NEGOTIATIONS

*By Hon. Willard Straight, Representative of the American
Banking Group*

It is the purpose of this paper to explain, if possible, three things: (1) the significance of Chinese loans; (2) the importance of securing and retaining an American interest therein, and (3), the peculiar difficulties encountered in the recent loan negotiations.

Dr. Arthur H. Smith, in that able and interesting work, *Chinese Characteristics*, pointed out that those who, understanding the vernacular, walk in China's streets will hear the passersby talk of little save money. As it has been with the daily life of the people so it is today with the political life of the nation. The question of money is all important. For the last ten years, and especially in the past twelve months which witnessed China's wonderful transformation from the oldest empire to the youngest republic in the world, there has been an incessant discussion of Chinese loans.

China's loan history may be divided into four periods:

The first, immediately after the Chino-Japan War—when funds were secured from abroad to pay the indemnity exacted by Japan at its conclusion.

The second, following the so-called "leasing years" when the great powers encouraged their bankers to finance railway construction in the regions which they had marked out as their spheres of special interest, and when besides acting as the politico-financial agents of their governments, these bankers secured for the industry of their respective countries the orders for the materials required.

The third, following the Russo-Japanese War, when likin was pledged as security for loans and when a combination to

which the American group was later admitted was formed by British, German and French financiers for undertaking Chinese loans, and for sharing the orders for materials required for their construction.

The fourth, and present period, in which a combination has been effected between the four groups named above and Russian and Japanese interests, for jointly financing the reorganization of the Chinese government.

American bankers were first interested in Chinese finance in the second period, in the Hankow-Canton Railroad; for business, not for politics. Their rights were sold back to China who financed the repurchase by a loan obtained from the government of Hongkong, which thus for obvious political, because geographical, reasons, secured for British interests a preferential right to finance the construction of this road in case foreign capital should later be required.

During the third period the American group was organized and became associated with the British, German and French banking groups. The American group, moreover, greatly contributed to the successful formation of the combination which marks the fourth period, a combination which is the financial expression of John Hay's "Open Door" policy, and which makes of international finance a guarantee for the preservation, rather than an instrument for the destruction, of China's integrity.

Before discussing the most recent phase of China's loan negotiations however, and the manner in which the American group at the instance of the Department of State made its entry into this field, it is necessary briefly to review the history of the past few years, and to consider the factors in the creation of what has been called "Dollar Diplomacy."

Because of this so-called "Dollar Diplomacy," President Taft, and his Secretary of State, Mr. Knox, have been subjected to no small measure of criticism. The administration one hears has formed an unholy alliance with the Octopus; and Wall Street, the property scape-goat of our national political drama, is accused of seducing a reluctant and hitherto well-domesticated government into the maelstrom of international financial adventure.

As if this were not sufficient, sober and intelligent journals have demanded why American capital should seek foreign fields when there is so much work to be done at home. Others admitting the desirability of foreign investment and the possible necessity of diplomatic support for those who undertake it, have objected to the administration's assisting certain institutions in Wall Street instead of American bankers in general. It must be remembered, however, that the success of any association of American capitalists undertaking this business depends primarily on their being of such standing as command respect from financial groups abroad and upon their willingness and ability to bear the expense of representation through tedious and too often unremunerative negotiations. Without these qualifications American bankers are not equipped to become the instruments which our government requires to assist in the extension of our foreign trade.

Another section of the press hails each and every over-sea venture with indiscriminate enthusiasm and rhetorically preens the feathers of the Bird of Freedom, sneering at or condemning our rivals, and lauding American enterprise with an impartial disregard of the real facts.

There has been too much unjust criticism, too much unwarranted praise, and too general a lack of candid exposition and intelligent comprehension of the reasons for, and possibilities of, "Dollar Diplomacy."

"Dollar Diplomacy" is a logical manifestation of our national growth, and the rightful assumption by the United States of a more important place at the council table of nations. Our export trade is constantly increasing and foreign markets are becoming each year more and more necessary to our manufacturers. The new policy aims not only to protect those Americans already engaged in foreign trade but to promote fresh endeavor and by diplomatic action pave the way for those who have not yet been, but who will later be, obliged to sell either capital or goods abroad.

European diplomacy is engaged in solving a maze of complicated questions immediately political, ultimately commercial in character. France, Germany, Russia, Italy, Austria

and Japan are endeavoring to acquire fresh fields for colonization or to create preferential markets for their merchants. Great Britain with her world-wide possessions is involved directly or indirectly, in almost every international question that arises and with these powers too, diplomacy has for years been of the "Dollar" variety.

International rivalry of this character, however, is found only in those countries whose native administrations are either decrepit or which are still militarily too weak to secure that consideration, which, unfortunately, depends not upon international equity, but upon the power of self-protection. In such lands a government desiring to secure a market for its nationals must because of the pressure of its competitors either acquire territory or insist on an equality of commercial opportunity. It must either stake out its own claim, or induce other interested powers to preserve the "open door." There is no middle course. This is a statement not of benevolent theories, but of political facts.

The people of the United States do not desire fresh territory over seas. The policy of our government has been to secure for American merchants the "open door." American industry has until recently been too much engaged by our own domestic expansion seriously to set about the establishment of foreign markets. A far-seeing administration has therefore inaugurated a new policy, the alliance of diplomacy, with industry, commerce and finance.

This is "Dollar Diplomacy." It has been active in various ways. In South America it has aided our merchants and manufacturers. In Central America, politics have played a more important part, and the Department of State has attempted to bring about financial reform in these smaller republics, and to prevent the recurrence of the revolutions whose leaders have almost without exception been actuated solely by a desire to acquire control of the national revenues. In China certain very tangible results have been accomplished and it is to give a more accurate conception of this much discussed, but little understood subject, that this paper is written.

Prior to 1894, China had practically no foreign debt. In 1894-1896, however, she borrowed extensively from England, France and Germany, to finance the war with Japan, and to provide the indemnity which she was forced to pay at its conclusion. These loans were secured upon the collections of the Imperial Maritime Customs, a Chinese service under the control of that able Irishman, Sir Robert Hart. In 1898, however, China made a number of contracts for loans for railway construction, with British, German, French, Belgian and American syndicates. Under all these agreements the bankers were entitled to a certain share in the profits of the lines, which were themselves to be mortgaged as security for the loans, and provision was made in almost every case for joint foreign and Chinese management. The railway materials and rolling stock required were purchased from the manufacturers of the countries whose bankers undertook to issue these loans.

The cession of Formosa to Japan at the termination of the Chino-Japanese War, the occupation of Chinese territory by Russia, Germany, France and England, in 1897-1898 and the exchange of "diplomatic notes" between these powers regarding the protection of their respective interests in China, together with the signature of the railway agreements mentioned gave rise to a discussion throughout the European and American press of the imminent breakup of China and the partition of this ancient empire into "spheres of influence."

In China the broad significance of these events was probably appreciated by but few, even of the leading statesmen of the time, but these men, nevertheless, and the gentry and official classes throughout the provinces felt that their country was becoming dominated by the foreigner. Seaports had been wrested from them, and, not content with this, the strangers were binding their helpless motherland with rails of steel.

For some years prior to 1898, the Empress Dowager had been in comparative retirement. The attempt of the young Emperor, Kuang Hsü, however, under the advice of Kang Yu Wei, suddenly to introduce widespread reform, brought

this redoubtable lady to the front once more. Popular discontent, fomented by bigoted and ignorant officials was winked at if not encouraged by a court which feared that the extension of western influence might bring about administrative changes which would curtail their opportunities for illicit gain. The Boxer outbreak was the result, and in 1900 the reactionaries made one last attempt to sweep the foreigner into the sea. Peking was occupied by the allied troops, the Manchu court fled to Sianfu, and China was saddled with a fresh debt of about £60,000,000 to pay for her mid-summer madness. This was charged upon the Maritime Customs, upon certain likin collectorates and upon the salt gabelle.

In 1898-1899 the American Secretary of State, John Hay, anxious to prevent the partition of China and to protect the interests of general foreign trade against discrimination in the portions of Chinese territory already occupied by foreign powers, enunciated his "Open Door" policy. His proposition, favorably received at first and reaffirmed in the negotiations which followed the relief of Peking, won the adherence of other nations not because of any particular consideration for China but because of their mutual jealousy and their realization that partition would impose upon them responsibilities which they might find it difficult to bear.

They did not therefore surrender the ports which they had forcibly leased, but their acceptance of the "Open Door" doctrine nevertheless marked the beginning of a financial and commercial, rather than territorial, definition of their respective interests. The Russo-Chinese Bank had been created in 1895 as the chief instrument of Russian ambition in her Manchurian adventure. This institution and the Hongkong and Shanghai Bank, the Deutsch-Asiatische Bank, the Banque de l'Indo-Chine and the Yokohama Specie Bank, now became more and more generally recognized as indispensable financial means to the political and commercial ends of their respective governments.

In contrast to the peaceful rivalry in China proper, the situation in Manchuria became more and more threatening. Russia despite her diplomatic assurances to the contrary

did not evacuate this region occupied after the Boxer trouble. She persisted moreover in an attempt to acquire control over northern Korea as well, until Japan, avowedly the champion of China's integrity and the "Open Door" for the trade of all nations, declared war.

Relieved by the defeat of Russia Peking breathed more easily. This satisfaction, however, was short lived, for the Chinese soon became convinced that Japan not unnaturally intended to reap for herself and not assure to China, the fruits of her splendid victory. She had taken from Russia the Liaotung Peninsula, from which she had herself been ousted after the China-Japan War. More than that, she succeeded to Russia's rights in the railway running north from Port Arthur and in the coal mines at Fushun.

When His Excellency Yuan Shih Kai, now President of the Chinese Republic, went to Tientsin as Viceroy of Chihli Province, he had with him a number of officials, notably Tang Shao Yi and Liang Tun Yen, who had been recalled from America in the early 80's, but who had not after their return to China been given much share in the direction of affairs. Yuan soon found himself at the head of what might be called a "Reform" party, and these subordinates of his, able, accomplished and well versed in American and European methods greatly aided him in instilling new force and intelligence into the Peking government. Administrative reforms were demanded, the Chinese press, hitherto practically non-existent, began to assert itself, and young men educated abroad returned to direct a "rights recovery" agitation which soon developed anti-Manchu propaganda and which found its final expression in the revolution of last year.

Peking became concerned about Japan's activity in Manchuria. Their Excellencies Hsü Shih Chang and Tang Shao Yi were sent to Mukden to establish, if possible, Chinese authority throughout the Three Eastern Provinces, and to exercise the right to develop this region under Chinese auspices, assured by the Portsmouth Treaty and the so-called Komura Convention, signed between China and Japan in the autumn of 1905.

They had no intention of interfering with the treaty rights acquired by Japan, but they wished, if possible, to induce

British, German, French and American capitalists to invest in the development of this region.

In the autumn of 1907, Lord French, representing Messrs. Pauling and Company, the well known firm of English contractors signed with the Manchurian Viceroy a contract for the construction of a railroad from Hsinmintun a point on the Peking-Mukden Railway, to Fakumen, with the ultimate object of extending this line north to Tsitsihar on the Chinese Eastern Railway. Japan protested on the ground that the construction of such a road would violate the provisions of the secret protocol attached to the Komura Convention, stipulating that China should build no railway parallel to or competing with, the South Manchurian Road.

Subsequently in the summer of 1908, His Excellency Tang Shao Yi signed a Memorandum of Agreement for a loan of \$20,000,000, to be undertaken by American capitalists for the establishment of a bank which was to act as the financial agent of the Manchurian administration for development work. This marked the beginning of the negotiations which led to the organization of the American group, the signature of the Chinchou-Aigun Railway loan agreement, the conclusion of the currency loan and the formation of the present six-power group.

In May, 1908, Congress had approved President Roosevelt's recommendation that the United States return to China a portion of the Boxer indemnity. Senator Root, then Secretary of State, and His Excellency W. W. Rockhill, then American Minister to China, suggested that the remitted funds should be expended in financing the education of Chinese students in the United States.

His Excellency Tang Shao Yi was appointed Special Ambassador, ostensibly to thank the American government for its generous action. His real mission was to negotiate the Manchurian loan with American bankers. On arriving in Washington, however, he advocated a much more comprehensive scheme. He proposed to Secretary Root that China should issue a loan of \$300,000,000 to be utilized for a program of industrial development, for currency reform, and to finance the Chinese administration during the period fol-

lowing the intended abolition of likin and until the consent of all the powers to an increase in the customs tariff was obtained. Mr. Tang desired an international loan in which he wished the United States to take the lead and Mr. Root promised to support this plan. With the authority of Mr. Root and the sanction of President Roosevelt the matter was brought to the attention of American bankers, but it was necessary temporarily to abandon the project owing to the dismissal of His Excellency Yuan Shih Kai from the high office which he then held in Peking.

Following the inauguration of Mr. Taft, however, the President and Mr. Knox became keenly interested and the Department of State desired, as soon as an opportune moment should arise, to reopen the question of customs revision and likin abolition, as well as currency reform, in accordance with the stipulations of our commercial treaty with China of 1903. With a view to taking up the proposed loan at the proper time, the American bankers, who have been interested, closely followed the situation.

In May, 1909, it became known that the British, French and German financial groups were about to conclude an agreement, to be secured on provincial revenues, for the construction of the Hukuang Railways, i.e., the lines from Hankow into Szechuan and from Hankow to Canton.

The Department of State held the promise of the Chinese government that if any foreign money were required for the construction of the Hankow-Szechuan Line one-half should be secured from American and one-half from British capitalists. The fact that internal taxes, upon whose abolition the contemplated increase of the Maritime Customs tariff depended, were being pledged as security for the new railway loan, directly affected the fulfillment of the engagement which the Department of State had made to assist China in obtaining from the other powers their consent to customs revision.

In order, therefore, that the United States might be entitled to a practical, and not merely a theoretical, voice in this matter, as well as to assure to American manufacturers a share in the profits of Chinese railway construction and the

business arising therefrom, it was essential that representative American capitalists should participate in the Hukuang loan. The Department of State offered this opportunity to the bankers already interested in the loan proposed by Mr. Tang Shao Yi and the American Group was organized creating an instrument which it was hoped might enable the Administration not only to further the interests of American trade but effectively to assist China in obtaining the consent of the powers to the customs revision she so greatly desired.

In the autumn of 1909, immediately following the organization of the American Group, a preliminary agreement was entered into with the Viceroy of Manchuria, by the American group and Messrs. Pauling and Company, for the construction of the Chinchou-Aigun Railway. Much has been written regarding this subject and in Europe especially, our government has been criticised for the so-called Manchurian "Neutralization Proposals" advanced toward the close of 1909, and which were politely declined by Japan and Russia at the beginning of the following year. Although the story of the inception of this project does not perhaps fall directly within the scope of this paper, it may be well here to recite certain facts in connection therewith which, had they been known, might have given a very different complexion to journalistic comment at the time.

The scheme of bringing the Russian and Japanese railroads in Manchuria under the control of a great international company was first conceived by the late Mr. E. H. Harriman, as a factor necessary to the realization of his dream of creating a "round the world" transportation system.

At the close of the Russo-Japanese War, Mr. Harriman visited the Far East. In September, 1905, working closely with the Hon. Lloyd Griscom, then American Minister to Japan, he drew up with the late Prince Ito and Count, now Prince, Katsura then Premier of Japan, a memorandum stipulating that the portion of the Chinese Eastern R. R. from Kwangchengtze to Port Arthur and Dalny (now known as the South Manchurian Railway), which had been acquired by Japan from Russia under the provisions of the Ports-

mouth Treaty, should be financed by an American loan and operated under joint Japanese and American direction.

This project was never realized. It was blocked by the late Marquis Komura, who raised what appeared to be insuperable objections to Mr. Harriman's plan.

Mr. Harriman however did not give up his idea. Agents of the Russian government during 1906-1907 proposed to certain American bankers that they purchase from Russia the portion of the Chinese Eastern Railway which remained in Russian hands at the end of the war, i.e., the line running across northern Manchuria, with its branch from Harbin south to Kwangchengtze. The Russians stated that they were willing to sell in case Japan also could be persuaded to dispose of the South Manchurian Railway.

In this connection it should be remembered that the agreement between China and the Russo-Asiatic Bank for the construction of the Chinese Eastern Railway, provided that China might repurchase the line after 36 years and that it would in any case revert to China at the termination of an eighty-year period.

Japan under the Komura Convention had been recognized by China as successor to the Russian rights, under this agreement, to the portion of the road acquired after the war.

It was proposed therefore that an international syndicate should anticipate the operation of this clause and repurchase the line on China's behalf, at this time, rather than later.

The scheme was discussed with Mr. Tang, during his stay in Washington, in the autumn of 1908 and he expressed the opinion that China would be glad to coöperate. An important Japanese financier who had been informally advised of the plan, however, stated that Japan would be unwilling to acquiesce therein.

Notwithstanding this fact the negotiations with Russia were continued and, in the summer of 1909, Mr. Harriman, through a leading Paris banker, approached M. Kokovtseff, then Minister of Finance, now Premier, of Russia, and was assured that on his return from a trip to Vladivostock, upon which he was about to start, M. Kokovtseff would recom-

mend the sale of the Russian Railway. This he did in a public address on his return to Moscow.

The existence of the Harriman memorandum, and the attitude of the Russian Minister of Finance aside from the broader political considerations involved, justified the American proposals. An entente had been arranged between Japan and Russia, however, in 1907. Both powers were greatly disturbed by the neutralization scheme and thanks to the understanding reached by M. Isvolsky the Russian Minister for Foreign Affairs, and Baron Motono the Japanese Ambassador in St. Petersburg, they refused to join in Secretary Knox's plan. Russian objections to the Chinchou-Aigun project, as well as the conditions imposed by Japan as precedent to her participation therein, moreover prevented the construction of this road.

Furthermore lest there should be any further misunderstanding as to their attitude these powers in the convention of July 4, 1910, agreed jointly to safeguard their respective interests in Manchuria—an arrangement which, though undoubtedly a natural one, was not, it must be admitted, calculated to assure to China herself the right to develop this territory.

In May, 1910, an arrangement was reached with the French, German and British groups for the participation of the American group in the Hukuang loan. At this time the three groups first mentioned invited the American group to join them in the combination which they had effected the year before for undertaking Chinese loans.

This invitation was later accepted and an intergroup agreement was signed in November, 1910.

On October 27 of that year the American Group had concluded a preliminary agreement for a £10,000,000 loan, to finance China's currency reform and to undertake certain industrial enterprises in Manchuria.

When the American Group was first organized, and actively supported by the State Department, was seeking participation in the Hukuang loan, Secretary Knox had declared that the American Government believed that the interests of China and of international trade with that country could best

be served by the friendly coöperation of the great lending nations and their banking groups.

It was in pursuance of this policy that the American group entered into the combination with the other groups and admitted them to equal participation in the currency loan, the final contract for which was signed on April 15, 1911.

The final agreement for the Hukuang loan was also signed with China by the same parties on May 20 of that year.

In the present negotiations with China for the reorganization loan, as in fact in all loan negotiations during the past few years, the banking groups have found their greatest difficulty in the settlement of the question of "control." It may be well therefore before giving the story of the recent negotiations to review briefly the history of this much discussed term.

The word "control" has for some time commonly been used to denote the guarantees against improper expenditure of loan funds which the banking groups, in a greater or less degree, have insisted upon securing, to which the Chinese government has from time to time reluctantly agreed, and constantly endeavored to modify.

"Control" in the at present accepted sense of the word was first embodied in the agreement made by the Chinese government in 1898, with the British and Chinese Corporation, for a loan to the Imperial Railways of North China.

Under this agreement, and in several others concluded at about this time, the lenders, besides securing a first mortgage on the railway whose construction they financed, were entitled to a share in the profits of the line.

For this reason and also because of the inexperience of the Chinese in railway matters, the bankers required assurances that the loaned funds should be so expended that the mortgaged property would constitute a sufficient security.

They furthermore obtained a certain share in the management of these lines in order that there should be secured therefrom an adequate return (to a certain percentage of which the banks were entitled), and to prevent the administrative inefficiency and fraud which they feared if the operation of these railways were placed entirely in Chinese hands.

The original railway loan agreements embodying the provisions above described were all concluded prior to the Boxer outbreak of 1900.

The final Shanghai-Nanking and Canton-Kowloon Agreements (the Canton-Kowloon Agreement slightly modified the "Shanghai-Nanking" terms) confirming these stipulations were signed in 1904 and 1907 respectively. The Tientsin-Pukow loan agreement concluded in 1908, however, substantially altered these conditions.

Its signature marked the first recognition by the banks of the increasing efficiency of the "Young China" party. These men demanded the radical modification of the old loan terms. They considered "control" subversive of China's sovereign rights and flattered by the blandishments of rival foreign interests, they were determined to exact from the world a consideration similar to that accorded Japan after years of patriotic self-sacrifice and conscientious endeavor. The avowed purpose of these officials to weaken the hold of the foreigner on China was heartily applauded throughout the provinces. It served as a patriotic issue on which an appeal could be made to the masses and a cloak under which the provincial gentry could cover their real purpose, which was to restrict the extension of the Peking government's authority by railways built with foreign loans, or otherwise, and their determination that if foreign loans were made, the chances for speculation should not be monopolized by the metropolitan mandarins.

Under the Tientsin-Pukow contract the Chinese government, by a cash payment redeemed the right held by the banks under the original agreement signed in 1898, to a share in the profits of the railway. No mortgage on the line was given. The loan service was to be met from the earnings of the road or from certain provincial taxes; and in this agreement it was for the first time stipulated that, in case of default on the loan service, the hypothecated revenues should be administered by the Maritime Customs Service. The principle of joint management was abandoned. The banking groups, however, insisted that the Chinese government should employ foreign engineers for the con-

struction of the line, and during the life of the loan, and that requisitions on loan funds specifying the purposes for which these sums were to be applied should be signed by the director general. The construction accounts of the railway were to be open to examination by foreign auditors to be appointed by the banks. Under former loan agreements the auditors had been empowered to stop the withdrawal of funds in case the Chinese officials were found guilty of peculation. This authority was not conferred by the Tientsin-Pukow contract and the effect of this modification soon became apparent.

The so-called "Tientsin-Pukow" terms, however, did not prove to be an effective guarantee against "graft."

From the commencement of the construction of this line there have been numerous scandals, the most flagrant instance resulting in the degradation of the director general and a number of his subordinates. The cost of construction has far exceeded even the most liberal estimates, and the loan service will therefore constitute a heavy charge on the revenues of the line.

Owing to the unsatisfactory operation of the so-called "Tientsin-Pukow" terms, negotiations were conducted in the winter of 1908-1909 between the British, German and French groups and their respective governments with a view to reaching an understanding as to the degree of "control" to be demanded from China as a condition precedent to future loans.

There are different versions as to the exact course of events in China at this time. It is, however, sufficient to state that in conducting *pour-parlers* with the Chinese authorities for a loan to construct the Canton-Hankow Railway,¹ the representative of the British and Chinese Corporation at Peking refused to agree to "Tientsin-Pukow" terms and insisted on more effective "control." The representative of the German group, however, accepted these conditions and secured the contract. The diplomatic protests and recriminations amongst the bankers which followed resulted in a compro-

¹ British capital had obtained a "preference" for financing the construction of this road. (See § 3, page 2.)

mise under which the British and Chinese Corporation was subordinated to the Hongkong and Shanghai Bank, which with its French associates, combined with the German group, to negotiate a loan to cover not only the Hankow-Canton but the Hankow-Szechuan Railways. The agreement was initialled on the sixth of June, 1909, and the "control" provisions accepted by the banks were similar to those embodied in the Tientsin-Pukow Agreement.

The inclusion of the loan for the construction of the Hankow-Szechuan Railway in this operation entitled American interests to the participation which the American group eventually secured.

Rivalry between the British and German groups had enabled the Chinese in the original Hukuang Agreement to secure "Tientsin-Pukow" terms despite the fact that the operation thereof had demonstrated that more stringent "control" provisions were needed.

Furthermore, during the year which elapsed before an agreement was finally reached between the British, German and French groups and the American group, there was an ever-increasing "anti-loan" agitation in the provinces through which the Hukuang lines were to be constructed. Provincial railway companies² were formed and secured from the vacillating Peking government rights which violated the terms of the agreement initialled with the "Tripartite Banks," and in which the Chinese had agreed the American group should be given a participation.

The National Assembly, the forerunner of the proposed Chinese Parliament was convoked for the first time in the autumn of 1910. Its members from the outset interested themselves in the question of finance and showed a determi-

² Considerable sums, quite insufficient however to build the railways in question, were secured by popular subscription, and in Szechuan province by taxation also. Construction work was commenced, and abandoned, and in a number of well authenticated cases the funds obtained by the companies were either lost by the directors thereof, who speculated heavily in the Shanghai "Rubber Boom," or stolen by more simple and direct methods. The demonstrated inability of the provincial companies to do the work they had undertaken was used by the imperial government to justify its very sound policy of railway "nationalization."

nation to scrutinize government expenditures, which the bankers felt would serve to restrict, even though it might not prevent, official speculation.

The National Assembly, moreover, was entitled to pass upon all government loans and was known to be opposed to a foreign loan for the construction of the Hukuang railways by the central government, instead of by the provincial companies. Sheng Kung Pao, Minister of communications, was determined, however, to build the Hukuang lines, and in response to the protests of the Assembly he pointed out that in negotiating the loan in question, he was fulfilling an obligation entered into in 1909, prior to the convocation of the Assembly, by the Grand Councillor Chang Chih Tung. He was obliged therefore to adhere as strictly as possible to the terms of the original contract, and would not and could not have consented to any new "control" conditions at this time.

In this arrangement the bankers acquiesced, feeling that the punishment inflicted after the Tientsin-Pukow frauds and the surveillance of the National Assembly over the expenditure of loan funds, as well as the difficulties by which the central government was confronted, justified them in confirming the "control" provisions of the original agreement.

The Currency Loan was of a different character, coming under the head of "government" or "administrative" loans. Practically the only loans previously falling within this category had been required to pay indemnities abroad and there was no necessity therefore that the lenders should exercise "control" over their expenditure. The currency loan, however, was to carry out a definite program and not for general administrative purposes. The four banking groups now acting in harmony believed some form of supervision to be necessary, and it was thought that the "control" machinery devised for railway loans, could, with certain modifications be utilized for assuring the proper application of the borrowed funds under the currency reform program.

The Chinese had reluctantly agreed to various control provisions in railway loan agreements, but they feared

that to admit the principle of supervision over administrative expenditures would be to pave the way for foreign control over China's general finances. An arrangement was finally made, however, whereby China submitted to the groups her program of currency reform for their acceptance, and agreed to expend the loan funds only in accordance therewith, to publish quarterly reports of disbursements made, and to engage a foreign expert to assist the Bureau of Currency Reform.

The loan has not been issued but it is open to question whether this "control," in practice, would have prevented speculation, and insured the proper expenditure of loan funds, and the effective operation of the currency reform program.

Immediately following the outbreak at Wuchang, on October 11, 1911, which marked the beginning of the revolution³ in China the representatives of the four banking groups in Peking were approached regarding a loan to the imperial government. The Manchus, however, seemed unable to cope with the rapidly developing revolt and the groups were unwilling to advance funds to a government whose continued existence seemed problematical. Their governments moreover decided to observe absolute neutrality as between the contending factions and refused to approve any loans to either side. The financial history of the Revolution has been ably told by Mr. George Bronson Rea in the *Far*

³ It has been generally stated that the disturbances in Szechuan province in August and September last marked the beginning of the revolutionary movement. This is not the case except that the general unrest created thereby contributed to the rapid spread of anti-Manchu sentiment. The Szechuan agitation was directed against the "nationalization" of railways, and the banking groups therefore have been accused of being the indirect cause of the revolt. This again is not true. The agitation was not against railway "nationalization" which the most intelligent leaders of Chinese public opinion recognized as desirable, but against the manner in which it was carried into effect. Shung Kung Pao, the Minister of Communication, upon the signature of the Hukuang Loan Agreement took steps to repurchase the rights of the provincial companies in accordance with the "nationalization" plan. Incidentally, it is reported on the best authority, he bought up the major portion of some of the provincial bonds, and offered to redeem them at par. He did not acquire control of the Szechuan bonds and therefore offered only 60 per cent on the face value. Hence the riots.

Eastern Review and in this account those who are interested may read of the various negotiations, practically all of them unsuccessful, undertaken by both the imperial and republican authorities during this period.

The Prince Regent of China retired on December 6, 1911, turning over the reins of government to Yuan Shih Kai, whom he had dismissed three years before at a time when he stood out, as he does today, as the only man capable of coping with China's domestic troubles and the difficulties by which she is threatened from abroad.

The Emperor abdicated on February 12, 1912, and on March 10 Yuan Shih Kai was inaugurated as provisional president of the Chinese Republic.

The present loan negotiations with the Chinese government were commenced in the middle of February, when the acting Minister of Finance, His Excellency Chou Tzu Chi, approached the representatives of the so-called "Four Groups" (i.e., British, German, French and American) at Peking, and asked for an immediate loan.

On February 26, Mr. Tang Shao Yi, representing the republican authorities at Nanking, arrived in Peking for the purpose of arranging a coalition government. On the following day, at Mr. Tang's invitation, the representatives of the four groups discussed with him the question of the loan broached some days before.

Mr. Tang stated the immediate requirements of the Chinese government, and requested the representatives to ask their groups to finance the same. In addition he discussed the Chinese revenues available as security for a large loan to reorganize the Chinese administration, and to initiate a scheme of commercial and industrial development. He asked the representatives how much China could borrow on this security, and finally, himself suggested the figure of £60,000,000, which he wished the banks to loan in five annual instalments of £12,000,000 each.

Pursuant to Mr. Tang's request for an immediate advance, the groups on the following day paid in Shanghai the sum of Taels 2,000,000, to meet the urgent requirements of the Nanking authorities.

The four representatives had reported Mr. Tang's request to their principals in Europe and America.⁴ No reply had been received when on the night of February 29 a number of the Chinese troops quartered in Peking mutinied, looted and burned portions of the city, and openly defied the authority of the provisional government. On the following day, March 1, it was suggested to Mr. Tang that it would be desirable that he should make some statement to reassure the groups who were considering his proposition, regarding the probable effect of the outbreak, and the ability of the government to cope therewith.

Mr. Tang's explanation was unsatisfactory, and the burning and looting continued on the night of March 1. On March 2, acting under instructions from Yuan Shih Kai, the acting Minister of Finance, requested from the four groups an immediate advance of 1,015,000 taels. He stated in his letter that the President appreciated that in view of the critical state of affairs in Peking, the groups would not be prepared to lend this money without the authority of their governments, and requested the representatives to secure the necessary sanction from their ministers as soon as possible.

Though Mr. Tang in order to justify the signature of the "Belgian loan" subsequently stated that the groups had refused to render assistance when approached after the mutiny of February 29, no other requests for immediate advances other than that mentioned above was received by the groups at this time.

The seriousness of the situation at this time is shown by the fact that on the same day Mr. Tang Shao Yi had addressed a note to the British Minister stating that he feared the Peking authorities would no longer be able to control the situation, and requesting the Diplomatic Corps to take

⁴ A number of writers on this subject have stated that on February 27 the group representatives made a definite agreement to furnish certain sums. This is not true. The group representatives merely agreed to report Mr. Tang's proposition to their principals. They did, however, in view of the urgent need of funds in Nanking (it was feared that the troops might mutiny if not paid immediately) themselves assume the responsibility of making the advance of Tls. 2,000,000, referred to in the final paragraph of the preceding page.

steps to assist the Chinese in preserving order. Yuan Shi-Kai later denied having authorized Mr. Tang to take this action.

On March 9 the necessary authority having been received from the four governments, the groups advanced the sum requested under an exchange of letters, which (1) assured to the groups the firm option for furnishing "the further monthly requirements of the Chinese government for the months of March, April, May and June, and if necessary, July and August," and (2) in view of the assistance rendered the Chinese government in advancing the sums mentioned above as well as in undertaking the contemplated advances for monthly requirements and maintaining Chinese credit on the markets of the world (by paying Chinese loan interest coupon charges which the Chinese government itself had been unable to meet), the Chinese government assured to the groups the firm option on the reorganization loan (provided their terms were equally advantageous with those otherwise obtainable).

From the proceeds of this projected reorganization loan it was intended to redeem the treasury bills, which were to be issued to cover the advances.

So urgent were the needs of the Chinese government, that the four groups did not at this time arrange the terms upon which they would discount these bills, it being impossible to settle this point until after the conference in Europe of the four groups, which had been called for March 12.

The terms on which the groups were prepared to undertake this business were not, however, communicated to the Chinese authorities, for on the evening of the 14th the four representatives learned that an agreement had that morning been concluded with the so-called "Belgian group" for a loan of £1,000,000, carrying an option for a further large loan.⁵

⁵ The Belgian loan was secured on the Peking-Kalgau R. R. the earnings of which together with the earnings of other "productive enterprises" controlled by the Board of Communications, had been pledged as security for the Anglo-French loan of 1908. The British and French Ministers successfully protested against the alienation of this security. The price paid by the bankers for the Belgian loan was lower than that which the four groups were ready to give—but there were no "control" provisions in the contract.

This transaction was completed at a time when the President and Mr. Tang knew that the representatives were hourly expecting a definite reply from the four groups to the proposals made by Mr. Tang on February 27.

The signature of the "Belgian loan" was virtually the first official act involving the new administration's relations with foreigners. It was a clear breach of contract. The groups, more especially the British, French and German, had since the outbreak of the Revolution in October, been themselves advancing funds to pay interest charges on Chinese loans which they had issued. They had done this to protect the public to which they had sold Chinese bonds, and to protect the credit of China where they had very large vested interests.

Despite the chaotic conditions throughout the provinces, and the absence of any really effective authority in Peking the groups with the support of their governments had been ready to advance to China funds sufficient to put the Peking administration on its feet at a time when no public issue of Chinese bonds was possible, in order to do their part in assisting the restoration of stable conditions.

The signature of the Belgian loan, however, affected the security for the large loan which the groups had been asked to undertake—and it carried no guarantee whatsoever that the funds furnished or to be furnished would be properly expended, it increased China's liabilities without insuring any increase in the effectiveness of her administration and instead of rehabilitating, it was calculated to prejudice, her credit.

The "Belgian loan" contract had been drawn subject to ratification by the "Advisory Council" at Nanking.

Despite the protest made by the four group representatives on March 15, Mr. Tang urged, and finally persuaded, the Council to ratify this agreement, on the ground that the four groups had refused to assist China after the outbreak of February 29. There is no evidence that Mr. Tang at this time informed the Council of the assistance which the groups had rendered, and were prepared to render, or of the existence of the letters of agreement of March 9.

The British, German, French and American Ministers on March 25 formally protested against the conclusion of the "Belgian" loan. Mr. Tang Shao Yi, then prime minister in the newly organized Cabinet, nevertheless attempted to secure further funds from the "Belgian" group. This failing, the Chinese government on April 15, replied to the Minister's protest describing the signature of the "Belgian" loan—and the violation of the letters of agreement of March 9, as a "misunderstanding" and requesting the ministers to instruct the group representative to resume negotiations with the premier on his return to Peking.

The four ministers refused to accept the explanation offered, and insisted that the government should admit its breach of contract with the four groups.⁶

This condition was accepted and negotiations were resumed. During the next few weeks the groups paid over further amounts, making the total sum advanced 12,100,000 taels, or approximately £1,800,000. Agreements covering these later advances were signed on May 17, and June 12 under which, after considerable difficulty, the Chinese had been persuaded to agree to the safeguards which the groups considered essential to assure the application of the loan funds to the payment of troops and to the other purposes for which they were borrowed.

At the request of their respective governments the original four groups with the approval of Yuan Shih Kai had agreed to admit banking interests designated by the Russian and Japanese governments, to a participation in these transactions, and after protracted and most delicate negotiations an agreement was reached between the six groups on June 20, 1912, in Paris, regarding the conditions upon which they were prepared jointly to undertake the proposed reorganization loan to China.

The groups were presented with the problem of financing

⁶ The "Belgian" group included the Russo-Asiatic Bank which was later designated by the Russian Government to participate in the "six power" syndicate. Under the Paris agreement of June 20, 1912, the members of the "Belgian" group were recognized by the combination as members of the "Russian" group.

the reconstruction of China on conditions which would be attractive to the bond purchasing public despite the disorganized condition of that country. To appreciate the difficulties the six groups were obliged to take into consideration, it is necessary to summarize the situation existing at this time.

They had been requested by China to furnish roughly 10,000,000 taels or £1,300,000 a month for six months and to provide other sums making the aggregate amount to be advanced 80,000,000 taels or about £10,000,000.

It would have been impossible to issue a Chinese loan at this time except at a figure so low as to prejudice the quotations for Chinese bonds already on the market, in the hands of the public not of the groups. To furnish the sums immediately required therefor the banks would have been obliged to discount treasury bills, which they would have either had to hold themselves, or dispose of to a very limited *clientele*.

These advances were required to pay the army, to finance the disbandment of superfluous troops, and to meet the current expenses of the government. The large loan was to be expended to redeem the treasury bills, to clear off arrears in China's indemnity and loan services, and to meet certain pressing outstanding obligations. Mr. Tang proposed to use the balance to make up the loss of *likin*, which he desired immediately to abolish, pending the consent of the powers to an increase in the customs tariff. In addition he had certain vague schemes for railway construction, afforestation, and the establishment of mills of various sorts.

For the advances and large loan requested the Chinese government proposed to pledge the salt gabelle as security. The service of the Boxer indemnity is a first charge on this revenue. It was estimated however that it now yields Taels 47,000,000 per annum—and could be increased to at least half as much again if honestly collected.⁷

⁷ Experience at Tientsin and Tsingtao has shown the enormous increase that might be obtained were this tax properly administered. In Tientsin a single station collected in six months as much revenue as the entire district had yielded in a year. At Tsingtao the collections of a station placed under foreign direction were at once increased six-fold.

The Chinese government at this time was powerless to collect the taxes which it offered as security and was unable to meet her indemnity and loan payments, to pay troops or to finance its current administrative expenses and its permanence was by no means assured.

During the course of the negotiations, from February to June, the Chinese officials had shown little appreciation of the magnitude of their financial task and had evinced little ability in dealing effectively therewith.

The groups nevertheless had advanced 12,100,000 taels in order to enable the administration to meet its most urgent needs and to prevent the disorders and mutinies which it was feared would occur unless funds, which the government could not secure from its own people, were obtained.

These advances had been made subject to certain conditions to insure their proper application to the purposes for which they were borrowed yet the Chinese officials charged with their expenditure had placed every obstacle in the way of a proper and efficient audit, to which they had agreed.

Patriotic Chinese, proud of their Republic and hopeful and confident of its future may regret the necessity of including such facts in this statement. These men, however, if they be fair minded, must admit that the banking groups, no matter how friendly they might be to China, would not have been warranted in disregarding them.

Because of these facts the groups were unwilling to undertake the business without the joint support of their respective governments. Because of these facts, moreover, they deemed it possible to proceed with advances and to undertake the reorganization loan only on certain conditions which were briefly as follows:

1. That the groups should have the right to satisfy themselves as to purposes for which funds were required.
2. That China should herself create a system of audit in which foreigners should be employed with powers not merely advisory, but also executive so as to ensure the effective expenditure of loan funds borrowed for the purposes specified.
3. That the salt taxes to be hypothecated for the service

of this loan should be administered either by the existing Maritime Customs organization or by a separate Chinese service like the customs, however, under foreign direction, thus safeguarding the proper administration of the security despite the possible continuation or recurrence of unsettled conditions in China.

4. That the groups should take the first series of the loan of £60,000,000, at a fixed price, and be assured an option on the subsequent series at a price to be based on the market quotation of the first issue, thus giving China the benefit of any improvement in her credit.

5. That to protect the quotation of bonds issued and to assure a successful marketing of subsequent series China should not borrow through other groups until the entire loan of £60,000,000 had been issued.⁸

6. That for a period of five years China should appoint the groups financial agents to assist the administration in its work of reorganization.

These conditions were submitted to the Chinese government and in reply the group representatives in Peking were informed that it would be impossible to China to accept a loan on such terms. Negotiations, however, though interrupted, were not formally broken off, and from the end of June discussions were continued between the Chinese officials and the group representatives, but without result.

The difficulty was not a question of the price at which the bankers should take the bonds. It was the question of "control." The Chinese particularly objected to placing the salt gabelle under the Maritime Customs, or any foreign directed service, and to the creation of a proper audit department to appointing the groups financial agents.

It has of late years become the fashion, particularly among officials, who like Tang Shao Yi, and Liang Tun Yen served for a short time in the Maritime Customs to criticise Sir Robert Hart and his administration. Mr. Drew will give

⁸ In the contract for the so-called "Crisp" loan of £10,000,000 China agreed to a stipulation which virtually prevented her from borrowing, except through the Crisp syndicate, for the period of one year or until the loan had been issued in entirety.

you an account of the life and work of this man, one of the truest friends China ever had.

The younger men, however, forget his splendid service—they do not realize that he did much to save their country, for them, from foreign aggression, and it galls them to admit that for years the Customs Service has been, and is today, with the exception of the Postal Service, also a creation of Sir Robert Hart, the only branch of their entire government which can, if judged by western standards, be termed efficient.

The suggestion that the salt gabelle should be put under the Maritime Customs therefore was refused, nor would the Peking authorities agree to create a similar organization to undertake this work. Chinese and many foreign critics have pointed out that the Customs Service functions at the ports—and that it would therefore be unsuitable for the collection of internal revenue. The Postal Service, also under foreign direction, however, has been successful in its work, conducted throughout China, while customs officials have shown great ability in dealing with likin collectorates and in solving customs problems in the interior of Manchuria.

The groups have not insisted upon the exact form the proposed administration should take. They have, and do, believe that the salt gabelle does not constitute, and cannot be considered, an adequate security unless by placing these taxes under a Chinese government service—but with foreign direction, inspectors, and auditors—an efficient and honest collection be assured.

In the present state of China when the Peking administration has by no means established its authority—when cabinets are formed and dissolved with kaleidoscopic rapidity, when revenues are not being collected, and when there are large bodies of armed men throughout the country, ready at any time to break into open revolt—the groups felt that before engaging to undertake so large a loan as that requested they should be able to be in a position to guide and advise China in her reorganization work, the success of which depends primarily on sound finance. It was for this reason that they asked to be appointed financial agents.

Many of the leading men in Peking have privately recognized the wisdom of the groups' conditions and the advantages to be gained should China accept them. Officially, however, these gentlemen have not dared recommend their adoption, fearing that their political opponents might make any concession to the foreigner the excuse for stirring up an agitation which they would be powerless to quell.

Hoping to obtain less onerous terms the Minister of Finance in July last proposed that the groups should continue advances to be redeemed from a loan of £10,000,000.

This sum, however, would have been scarcely sufficient to meet China's outstanding and immediate obligations. The safeguards which were suggested by the Chinese moreover were inadequate. The groups therefore were unable to negotiate on this basis. The officials then stated that as the groups would not lend on "reasonable" terms they would be obliged to secure funds from their own people. The group representatives and the foreign ministers in Peking welcomed the suggestion, and urged them to make a "popular" loan. This was attempted but without success; the "people" contributed small sums, but not enough. The government next approached certain commercial houses and secured small loans, in return for large contracts for arms and ammunition. Tramway concessions were offered in return for cash advances, and other expedients adopted to secure funds sufficient to meet the government's running expenses, all of which while relieving a temporary necessity merely increased the difficulties of an already almost hopeless financial problem.

Early in September it was reported that on August 30 the Chinese Minister in London had signed a loan agreement with Messrs. C. Birch Crisp and Company of London. Enquiry addressed to the Minister of Finance in Peking evoked the information that he, the Minister of Finance, had had nothing to do with the conclusion of the London contract which had been arranged by his predecessor acting in an informal capacity. The Minister of Finance assured the representatives that China desired to deal with the six groups as the only combination capable of furnishing within

the next few years the enormous sums which China would need to reorganize her administration and finance the industrial development upon which the Peking Government wished to embark. At the time this discussion took place funds advanced by Messrs. C. Birch Crisp and Company had already been transferred to China and placed to the credit of the Chinese government in a Tientsin bank. This fact became known to the representatives who brought it to the attention of the Minister of Finance. He reiterated his former declaration that China desired to deal with the six groups and as late as September 23 handed the representatives a statement of conditions which he informed them China would be ready to make the basis for the continuation of negotiations for the reorganization loan. These terms were not considered acceptable by the group representatives. The Minister of Finance thereupon informed them that since they had refused the terms proposed by China he considered that the option which the groups had held, had lapsed and that China was free to negotiate with other parties. The so-called "Crisp" loan was issued in London shortly afterward.

From the above facts it would seem that the Chinese government was prepared to repudiate the contract signed with London bankers on August 30, in case the six groups were willing to come to terms.

This incident, in connection with others mentioned above, is not cited for the purpose of impugning the good faith of the Chinese government. Those familiar with the difficulties with which the provisional government has been endeavoring to deal are not inclined to hold China too strictly to account for what her real friends will regard as mistaken and unfortunate, rather than reprehensible, efforts to solve her financial problem. At the same time, with all possible consideration for China and every sympathy for her officials in the performance of their onerous tasks, it must be recognized that such actions will, if continued, make it impossible to maintain Chinese credit.

It will be said perhaps that by concluding the so-called "Crisp" loan, China demonstrated her ability to borrow in

the markets of the world. This may be true, but the fact that China could in this case secure funds was due largely to public confidence in the stability of the Chinese administration based on the willingness of the six-power group to advance funds to the provisional government even prior to the inauguration of the President, Yuan Shih Kai, and the belief that the six groups would in the end come to an arrangement with Peking which would give value to all Chinese securities.

Many gentlemen in the United States have pointed out in discussing this subject that the American banking group in particular should remember the history of our own country and not be too exacting in its dealings with the Chinese Republic.

The argument is plausible but cannot be given too much weight when it is remembered that when our federal government was first established there was no large public debt while the resources of the young American Republic were enormous. The funds secured from abroad during our revolution, and immediately following its conclusion, had been advanced by the French government, not so much with the idea of assisting the struggling colonies as for the purpose of embarrassing Great Britain. Only when Alexander Hamilton had reorganized the finances of the country, securing the assumption by the federal government of the larger part of the debt of the states, and after he had put the administration of the Treasury Department on a sound basis, were the United States able to borrow from foreign bankers on satisfactory terms. The Ministry of Finance in Peking, however, is still operated on lines scarcely conformable to our ideas of a business administration, despite the efforts of able men like Dr. Chen Chin Tao, while the republican government has assumed the obligations of its imperial predecessor for which the revenues of China are to a very large degree already hypothecated, and for the service of which they are at the present time insufficient.

Not long ago I happened to be present when the loan question was discussed by a distinguished gentleman who had just returned from the Far East. He had been greatly

impressed by what the revolution had accomplished, was full of admiration for the Chinese people and confident of the bright future of the Republic. He felt that the bankers were mistaken in demanding terms which the Chinese considered so onerous and thought that the wiser policy for the groups would be to work for the future by now making concessions calculated to relieve the Chinese officials of their immediate embarrassments. He thought that for American merchants the fairest, and at the same time the ultimately most profitable, attitude to adopt toward China was to strive for the maintenance of the "open door" under which with a strong central government international trade would greatly prosper.

He recognized that the authority of the present Peking administration was not generally established in the provinces, that revenues were not being collected and that without money the central government could not become strong. He admitted that while he had met many officials he had seen few whom he considered competent to direct the expenditure of large sums in the manner most likely to assure the speedy restoration of normal conditions throughout the country and he believed therefore that the Chinese government should employ advisers and accept their advice.

The distinguished traveler had predicated his hope for the future on the establishment of a strong central government which would be able to collect sufficient revenue to finance its own reorganization. Unfortunately, however, this cannot be accomplished unless the Chinese government first secures from abroad money sufficient to give it the power to make these collections and pay off its pressing debts under safeguards which will protect it for the time being from external aggression.

If his conclusions as to the ability of Chinese officials now in power were warranted, and his observations correct regarding the present state of affairs in China, his recommendation that the groups "play for the future," by lending money on terms acceptable to the Chinese, would scarcely seem justified by his premises. Those who have lived in China and grown to know and admire the Chinese, however, will readily

understand this point of view. It is impossible not to sympathize with the aspirations of the young men who are now striving to do what they can for their country. At the same time American bankers would not be acting as true friends of China if they failed to look the facts of the situation in the face. They would not be "playing for" the best future for China should they lend money on conditions which might satisfy the vanity of Chinese officialdom but instead of assisting the establishment of a strong central government would encourage improvident financial methods and lead inevitably to foreign intervention.

The present financial situation in China is set forth in an article in the *North China Herald* of September 28, 1912, an abstract of which is given below:

The obligations that China is bound to liquidate are as follows. First of all, Tls. 12,000,000 advanced by the sextuple group from February to July, on the distinct understanding that the Chinese government would sign the loan with them, including this sum in the total amount for which the loan is signed. The Chinese government gave the banks treasury bills, and at the exchange fixed the total works out at £1,750,000 sterling. Secondly, there are amounts due to the shipbuilding firms in England and the United States for works executed by them on orders given by the Manchu government but completed during this year. In the list of their outstanding debts furnished by them to the sextuple group the Chinese government have £700,000 against this item.

Thirdly, there are the Hupeh and Nanking loans of about £300,000 each given by the banks to the Viceroy of the two provinces on the authority of Peking during the Manchu régime. These sums have been overdue for some time, and as the new government has undertaken responsibility for all the past obligations they must be paid the moment it obtains funds. Fourthly, there are two loans contracted at recent dates on the understanding that they would be repaid as soon as China signed the big loan. The Diederichsen loan of Mks. 5,000,000 and the Carlowitz loan of Tls. 6,000,000 come under this category. Part of these amounts was received in cash, although the major portion consisted of amounts due on arms and ammunition supplied by these firms during the revolution.

Fifthly, the Skoda loan contracted with Arnold, Karberg and Company during the revolution, the moiety of which was received in cash and the rest in the shape of arms and ammunition, amounts to about £450,000. Sixthly, as the currency loan was floated by members of the group, and as it is not likely to be floated by them if the present arrangements are continued, they will be entitled

to demand repayment of the advance of £400,000 made to the government last year in April, 1913.

In the seventh place, the amounts due on indemnities, which have been outstanding since October last will work out at over £2,500,000. The total to be paid by China on this account works out roughly at £250,000 per month. Making due allowance for last year's surplus from the customs revenue and the accumulation of native customs revenue, which Dr. Morrison referred to recently, there would still be outstanding the amounts due from January this year.

Lastly seeing that the Chinese dropped the Anglo-Belgian syndicate loan after taking an advance of £1,250,000, the syndicate will not have the least hesitation in demanding immediate payment of the amount. Besides there are a number of small Japanese loans, and small German loans, other than those we have mentioned, mostly for arms supplied during the revolution—the date of payment of which is long overdue. Everybody has been anxiously waiting for the big loan, especially as no security has been given besides the bond of the Chinese authorities.

Further, it is necessary to state in this connection that the merchants, banks and other rich Chinese who helped the new government, both during the struggle and after, now stand badly crippled from want of funds. They have been often told that their outstandings would be cleared as soon as the first loan with the foreigner was closed. Trade is badly in need of the funds spent on the revolution; and if a moiety of the debts of the government is not paid even after a foreign loan becomes an actuality, the failure may give rise to acute discontent. The amount on this score is not available, but the lowest estimate puts it at about Tls. 20,000,000.

Let us suppose that the London syndicate is able to float the whole of the £10,000,000⁹ in October. The loan is expected to be floated at 95, brokerage and other expenses incident on the flotation may be put at 3 per cent, and by the time the loan is floated, if at all successfully, China would have received and spent at least £150,000. The net receipts from the loan would therefore amount to £9,050,000. The total foreign indebtedness, of which China could not in honor delay payment, amounts to £8,950,000. Thus she will have a residue of £100,000 with which to pay her unpaid troops and disband them, and begin setting the Republic in order.

If China refuses to pay all her outstanding debts at present except the indemnity instalments that have fallen in arrears—in order to save the salt gabelle from being taken over by the powers—she will have fully £6,500,000 to pay her soldiers with and begin reforms at once—so it is suggested in some quarters. In the case of an individual such refusal would mean bankruptcy;

⁹ £5,000,000 was floated in September. The bankers paid 89 for the bonds—China received not more than £4,450,000.

in the case of a nation it would mean the utter ruination of its credit in the markets of the world. And China must necessarily borrow much more than £10,000,000. There is no disguising the fact that China has no security to offer—security in the proper sense of the word. Her performances in the past have not been such as to inspire confidence. And her hidden resources need an enormous amount of capital in order that any tangible result may be got out of them.

It may be remembered that in his speech in March before the Assembly at Nanking the then Premier, Mr. Tang Shao Yi, stated that £25,000,000, besides the revenue, would be absolutely needed within the next twelve months. What he said then was substantially correct, and remains true today. The interval has only slightly added to the total needs, as the soldiers are still being kept and paid from want of funds to pay and disband them—although in the interim a number of small loans and advances have all been received and spent. It is quite interesting to note the different items for which funds are needed although our list is not identical with that supplied to the Assembly by Mr. Tang Shao Yi.

If China wishes to preserve her credit as a power, she must liquidate her pressing debts before beginning any constructive work. First and foremost is the foreign indebtedness to the tune of £9,000,000—the details of which we have mentioned above. Secondly, her merchants, bankers and gentry, who supplied funds to prosecute the revolution and carry on the new government deserve better consideration than they have received; and the sums owing to them are estimated at about Tls. 20,000,000, or roughly £3,000,000. Thirdly, she must pay the troops, who are now eating their heads off, and disband the major portion of them. It was estimated that expenditure on this score would cost £5,000,000 some four months ago. A certain number of troops have been disbanded, but the cost of getting rid of the rest of them has not greatly been lessened, owing to the delay.

Fourthly, she will have to buy back the republican bonds, on which she has to pay interest half yearly at the rate of 8 per cent per annum, while the bonds are continually depreciating. Sums received on account of the “so-called patriotic loan,” while of no practical utility to her, are depleting the resources of the trade in the provinces. These suggestions are made with the view to enable China to start with a clean slate, if she wishes to proceed with the work of reorganization without encumbrances. Thus before she begins any construction work she stands to have to pay out £19,000,000.

Now as regards sums needed for construction work and reform. The basis of all reorganization in China is currency reform, and so long as the currency is what it is there is no hope of making headway of any kind. It may be remembered that in the currency loan arrangement of 1911, £7,000,000 was set apart for currency reform; and that amount does not err on the side of extravagance. Whatsoever may be the final decision in regard to the

standard, there is no doubt that a considerable amount of silver would have to be purchased presently and coined; and one may rest assured that in working out the details in connection with bringing about a uniform currency throughout the length and breadth of the country, more funds may be needed later on.

Of equal importance is the immediate necessity for taking measures to minimize the effects of the famines and floods, which cause a perennial loss to the country and bring death and ruin to thousands, if not millions, year after year. Mr. Jameson's scheme of constructing dykes should be taken in hand immediately, and afforestation should be carried on simultaneously. An expenditure of £5,000,000 distributed during the next five years is not beyond the mark; and the loss averted during this period, judging by past experience, would be fully that amount. Of course, when a loan is arranged, it should be for the full amount, for the sooner the works are finished the more profitable they would be for the country. In so far as such expenditure would amply repay itself, it is hardly to be reckoned among China's debts. But it is a charge for which, in the first place, a large sum of ready money will be required.

The ideal of any loan to China at present should be to enable her to pay back the past and present borrowings. Of course, the basis of such an ideal are the untapped resources of China for taxation, the great industrial and agricultural possibilities of the land and the hidden resources of the country. But even to find these money is needed; to develop them much more. Development in this direction alone, under the aegis of a good government and a sound currency, would enable China to pay interest and principal of past, present and future debts. Expedients like those of the increase of the customs dues or the salt tax would prove only of temporary utility, and under certain conditions might even do harm.

The currency loan of last year included provision for £3,000,000 for Manchurian industrial development. And thrice three millions sterling for the eighteen provinces for industrial development and administrative reform would only err on the side of economy. Of course, this program does not take into account sums needed for railway construction in the country or private industrial enterprises. And in China's present financial state it would be ridiculous to dream of spending money for military or naval advancement. Thus, it would seem that if foreign loans should serve any beneficent purpose at all for China, a sum of £40,000,000 is necessary during the year ending, say, next June; and further amounts, into the details of which it is too early now to go, appear likely to be needed in the coming years.

This total of China's needs for the year is based on the supposition that the revenue of the country will meet its ordinary expenditure. Mr. Tang said there would be a deficit of Tls. 40,000,000 this year, and probably the same amount next—the obvious deduction being, of course, that borrowings will have to

be increased to this extent. Anyhow, there is no doubting that any syndicate proposing to lend money to China should be able to arrange for £40,000,000 during the next nine months, and be able to pay about £60,000,000 during the next three years. The original proposal of the sextuple group was arranged on this basis, and the total of £60,000,000 was agreed upon as necessary for the regeneration of the country.

Again it should not be forgotten that the annual payments on foreign loans by China will almost be trebled from 1916. The amortization of the railway loans starts from then, and the indemnity payments would then be more than double the present amounts. If China is not up and doing, with something in the way of reorganization she must be deeper in the mire than ever by 1916. At present everything in the way of reform needs large initial expenditure. To stop squeeze in the collection of revenue it is necessary to have good accounting, and officials with a salary which would place them above temptation. The land tax in China gives a ridiculously low yield; to increase it an effectual survey costing millions of taels is essential.

That the banks composing the sextuple group, with their respective governments at their back, would be able to supply China with this large total with more facility than any number of other syndicates is beyond question. The Chinese themselves know it, and hence their anxiety to keep on good terms with the group in spite of their latest action.

Apropos of the apparent success of the new loan we understand that already demands have been made upon Peking by several individuals and institutions in China. The funds of the Bank of China were drawn upon to further the cause of the revolution; and the bank naturally requires money to carry on its ordinary business. This bank is the best of institutions of a similar kind in China and deserves the help of the government—at least to the extent of receiving back what it paid out. But then, how far will £10,000,000 go?"

Such is the situation as seen by the Shanghai business man. The six groups because of the support of their governments, and because they believe that a loan properly safeguarded is the only means by which normal conditions can be restored in China, are willing to assist the Chinese government, in dealing with the conditions described above. They are criticised, however, because they are unwilling to loan funds except on terms which the Chinese regard as humiliating.

It has frequently been stated moreover that one of the chief Chinese objections to the "six-power" group has been the fear of any combination in which Russia and Japan is represented. Those who are familiar with Far Eastern

politics and who have considered their relation to European affairs, are aware that this grouping of the powers is a safeguard rather than a menace to China's integrity. They will realize that if this combination be maintained and China be willing to coöperate therewith, she will be able better to protect herself against the selfish designs of individuals which even though they may not be prevented will certainly be restricted by the necessities of joint action.¹⁰

Those who have criticised the attitude of the six-power group have in a measure lost sight of some of the elementary functions of a banking house which handles foreign loans. They have forgotten that it is not the bankers themselves who provide the money to finance a foreign loan, though they may for a time advance from their own resources certain preliminary payments. Bond issues, however, are sold to the public, the bankers receiving their commission on the sale and the reputation of a house of issue like that of any other commercial establishment depends upon the quality of the commodity which it sells. Bankers would not be justified in requesting their clients to take bonds on a sentimental and not a business basis any more than the president of an insurance company would be warranted in loaning funds for which he was responsible to a personal friend regarding whose solvency he had no guarantee.

The groups engaged in the present Chinese loan negotiations are institutions of the highest standing in their respective countries. The rupture in negotiations did not come because the bankers attempted to obtain an unreasonable commission but because they felt they could not afford to place upon the market a loan which they did not consider sound in the present state of China unless they obtained safeguards such as they have demanded, not to add to their own profit, but in the interest of the prospective investor.

¹⁰ Had it not been for the agreement between the six powers to take no separate and individual action during the Revolution Japan would have sent an expedition to China to keep the Manchus on the throne. She was prevented from taking this step by the representations of the British government which insisted that nothing should be done to prejudice continued joint action by all the great powers.

Fair-minded observers of recent events in the Far East recognize that the American banking group has during the past three years demonstrated its friendship for China. The American bankers personally wish for the success of the Chinese Republic. As real friends of China, however, it would be just as reprehensible for them to offer for sale bonds secured from China on terms which they did not consider calculated to restore and increase her credit, as it would be for them to issue to the public securities which they did not feel assured would constitute a sound investment.

It has been stated by men in authority in Peking that they would rather sell their country bit by bit than submit to the terms asked by the six-power group. Concessions have been offered giving to foreigners the right to construct and operate railways for forty years in return for a cash down payment of 5,000,000 taels. This indeed would be to sell the nation's birthright for a mess of pottage and to sow the dragon's teeth of financial bondage. Yet it is proposed by the very men who complain most bitterly of the conditions required by the six groups which are mild in comparison and which are calculated to build up a strong central government rather than create a nest of warring foreign interests which will cause China trouble and shame for years to come.

In these negotiations the banking groups have been charged with a very heavy responsibility. Their terms were submitted only after long and careful deliberation. China's difficulties were fully and sympathetically considered and the conditions required by the groups were prepared in her interest as well as in the interests of the groups and the prospective bondholders.

Recognizing, however, the peculiar difficulties of the present Peking government the groups have throughout been willing to consider any plan which the Chinese themselves might propose, calculated to free them from embarrassment, and at the same time carrying with it safeguards sufficient to make any loan based thereon a sound investment.

The six groups have been endeavoring to induce China to undertake real constructive work while the Peking authorities have either failed to realize the necessity therefor or

have been unwilling to assume the responsibility of undertaking a practical and comprehensive scheme. In following this course these officials are China's worst enemies for the reckless financial policy of the past few months if continued will lead to that very intervention, which in refusing the six groups' terms, these gentlemen have been avowedly trying to avoid.

The groups have not been attempting to force money, with humiliating conditions attached, on China. They have stated merely that they are willing, only upon certain conditions, to loan the money which China has requested them to furnish. The groups do not insist that China accept a loan if these conditions are unacceptable. They do say that they will not issue Chinese bonds on terms which they regard as unsatisfactory. The "six-power" groups do not constitute a monopoly but they are not willing to undertake any loan unless assured that they will be entitled to furnish on sound conditions funds to complete the transactions, the initiation of which they finance, and that they shall have a clear market until the different loan series for which they contract are sold.

For the sake of the preservation of China's integrity and the commercial "open door" it is to be hoped that some mutually satisfactory understanding may be reached between China and the "six-power" group. It is to China's interest that this combination should be maintained, and it is to the interest of China as well as of the United States, that we should retain our present position therein. China's great problem to-day is that of finance. It is to her advantage that we are entitled to a practical voice in its solution, and it is to the advantage of American trade that the United States continue to be an active party in Chinese loan negotiations.

SUPPLEMENTARY NOTE

Although the agreement for the Reorganization Loan was on the point of signature early in February, developments since that time have caused a further postponement of the conclusion of this transaction.

The terms agreed upon by the Chinese government and the bankers are substantially those outlined in the foregoing pages. The purposes for which the money is to be expended were specified by the Chinese government and deemed satisfactory by the bankers.

Provision has been made in the loan agreement to ensure the expenditure of borrowed funds for these specified purposes. The Chinese government has itself established an Audit Department and engaged to appoint a competent foreigner to introduce an effective system of accounting, while a Bureau of Foreign Loans will also be created which will, like the Audit Department, be under the direction of a foreign employee of the Chinese government.

The proposed agreement also stipulates that the Chinese government shall appoint a foreigner who shall act jointly with the Chinese Director General of the Salt Administration and provision is made for the appointment of foreign and Chinese district inspectors, who shall have charge of the salt production, the sale of this commodity to the salt merchants and the collection of the salt revenues, which it is stipulated shall be deposited with the group banks until provision is made for the service of the loan. The loan agreement also contains a provision, which, if the six groups undertake the reorganization loan, will protect the market therefor until it has been issued in entirety.

The negotiations resulting in the preparation of the agreement outlined above were undertaken by the banks on the understanding that the Chinese government would appoint foreigners to the positions mentioned and would satisfy the six legations in Peking that these employees would be engaged under contracts which would enable them to render effective service.

The Chinese government on the night before it was expected that the loan agreement would be signed nominated a Dane for the Salt Administration, an Italian for the Audit Department, and a German for the Loan Bureau. Certain of the interested governments desired that these foreign employees should be of the nationality of the lending bankers. These points were raised at the last moment and re-

quired a month to adjust between the various governments concerned. The program agreed upon by the six governments was submitted to the Chinese government early in March and refused by the Chinese. At the time of writing, however, negotiations are still in progress and it is to be hoped that a mutually satisfactory arrangement will soon be reached.

EDITORIAL NOTE

Since Mr. Straight completed this article, the American Banking Group has definitely withdrawn from further participation in the Six Power loan negotiations, due to President's Wilson's refusal to continue the moral support of the Government. The following are the official explanations of the attitude of the Administration and of the American group respectively. President Wilson gave this statement to the press:

We are informed that, at the request of the last administration, a certain group of American bankers undertook to participate in the loan now desired by the government of China (approximately \$125,000,000). Our government wished American bankers to participate along with the bankers of other nations, because it desired that the good will of the United States toward China should be exhibited in this practical way; that American capital should have access to that great country and that the United States should be in a position to share with the other powers any political responsibilities that might be associated with the development of the foreign relations of China in connection with their industrial and commercial enterprises. The present administration has been asked by this group of bankers whether it would also request them to participate in the loan.

The representatives of the bankers through whom the administration was approached declared that they would continue to seek their share of the loan under the proposed agreements only if expressly requested to do so by the government. The administration has declined to make such request because it did not approve the conditions of the loan or the implications of responsibility on its own part which it was plainly told would be involved in the request.

The conditions of the loan seem to us to touch very nearly the administrative independence of China itself; and this administration does not feel that it ought, even by implication, to be a party to those conditions. The responsibility on its part which would be implied in requesting the bankers to undertake the loan might conceivably go the length in some unhappy contingency of forcible

interference in the financial, and even the political affairs of that great Oriental state, just now awakening to a consciousness of its power and of its obligations to its people.

The conditions include not only the pledging of particular taxes, some of them antiquated and burdensome, to secure the loan, but also the administration of these taxes by foreign agents. The responsibility on the part of our government implied in the encouragement of a loan thus secured and administered is plain enough and is obnoxious to the principles upon which the government of our people rests.

The government of the United States is not only willing, but earnestly desirous of aiding the great Chinese people in every way that is consistent with their untrammelled development and its own immemorial principles. The awakening of the people of China to a consciousness of their possibilities under free government is the most significant if not the most momentous event of our generation.

With this movement and aspiration the American people are in profound sympathy. They certainly wish to participate and participate very generously, in opening to the Chinese and to the use of the world the almost untouched and perhaps unrivalled resources of China.

The government of the United States is earnestly desirous of promoting the most extended and intimate trade relationships between this country and the Chinese republic. The present administration will urge and support the legislative measures necessary to give American merchants, manufacturers, contractors and engineers, the banking facilities which they now lack and without which they are at a serious disadvantage as compared with their industrial and commercial rivals. This is its duty. This is the main material interest of its citizens in the development of China.

Our interests are those of the open door—a door of friendship and mutual advantage. This is the only door we care to enter.

The following was handed to the press by the American group, March 19:

The American Group, consisting of J. P. Morgan & Co., Kuhn, Loeb & Co., The First National Bank and the National City Bank, was formed in the spring of 1909, upon the expressed desire of the Department of State that a financial group be organized to take up the participation to which American capital was entitled in the Hukuang Railway Loan Agreement, then under negotiation by the British, French and German banking groups.

This group thus became interested in Chinese Loan matters, not primarily for its own profit, but for purposes indicated by President Taft and Secretary Knox. As stated in President Taft's message to Congress of December 1909, these purposes, in effect, called for the co-operation of the bankers as the "indispensable instrumentality" which the American Government needed to enable it

"to carry out a practical and real application of the open door policy." The Department of State considered that American co-operation with the Banking Groups of the several great powers enabled the United States to exercise a practical voice in China's affairs and constituted the best guarantee for the preservation of China's integrity.

In pursuance of the policy so advocated, the American Group, with the Administration's approval, entered into an agreement with the British, French and German Groups for the purpose of rendering financial assistance to China. In February 1912 these four groups at the request of their respective Governments and with the consent of the Chinese Government, admitted Russian and Japanese financial groups to the negotiations for the Reorganization Loan, thus constituting what has since been known as the Six Power Group.

Following the revolution and despite the fact that the authority of the new Republic had not been generally accepted, the American Group joined with the other groups in making to the Provisional Government substantial advances to enable it more firmly to establish its authority and to restore normal conditions throughout the country.

Meanwhile there had been in negotiation, during a period of many months, a loan agreement which, in its general terms, appeared last month to meet the approval of the Six Governments, of their banking groups, and the Chinese Government, and to be ready for signature.

These terms were intended to cover two points. The first was to enable the Chinese Government to reorganize its administration on an effective modern basis, to pay off its large outstanding debts and build up Chinese credit. The second was to protect the interests of American and European investors. For such protection, in the judgment of the Governments and the Groups, the only method was to ensure, despite any possible recurrence of political unrest in China, the proper expenditure of the funds loaned to China and to safe-guard the handling of the revenues pledged for principle and interest of the bonds.

As announced in the statement given to the press yesterday the present Administration at Washington, with a desire to be of assistance to China and to promote American interests in the Far East, has decided that these purposes may better be served by the adoption of a different and independent policy. As the American Group had been ready to serve the Administration in the past, irrespective of the heavy risks involved, so it was disposed to serve the present Administration if so requested. But deferring to the policy now declared, the Group has withdrawn entirely from the Chinese Loan negotiations and has so advised the European and Japanese banking groups.